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Federal Communications Commission
Office of Secretary

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January 29, 1997

Mr. William F. Caton
Secretary
Federal Communications Commission
Room 222
1919 M Street, N.W.
Washington, D.C. 20554

DOCKET FILE COPY ORIGINAL

**Re: Access Charge Reform, CC Docket No. 96-262; Price Cap
Performance Review for Local Exchange Carriers, CC Docket No.
94-1; Transport Rate Structure and Pricing, CC Docket No. 92-
213**

Dear Mr. Caton:

Enclosed herewith for filing are the original and sixteen (16) copies of MCI Telecommunications Corporation's Comments regarding the above-captioned matter. Pursuant to the Commission's request, MCI is also submitting a 3.5 inch diskette using MS DOS 5.0 and WordPerfect 5.1 software, containing our enclosed comments.

Please acknowledge receipt by affixing an appropriate notation on the copy of the MCI Comments furnished for such purpose and remit same to the bearer.

Sincerely yours,

Bradley Stillman

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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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Transport Rate Structure and Pricing)	CC Docket No. 92-213
)	
Usage of the Public Switched Network By Information Service and Internet Access Providers)	CC Docket 96-263
)	

COMMENTS OF MCI COMMUNICATIONS CORPORATION

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January 29, 1997

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Attachment: Kwoka Affidavit

Summary

In the instant proceeding, the Commission embarks on the final chapter of the competitive trilogy. The three proceedings that make up the trilogy -- interconnection, universal service and access reform -- are each critical to achieving the ultimate goal of a fully competitive local telecommunications marketplace which provides the public with lower prices, increased innovation, and ever-improving service. The access charge proceeding, however, presents an opportunity for the Commission to provide a consumer benefit -- lower long distance prices -- right now. The fact that this action would also help bring competition to the local monopoly market makes any other action both a missed opportunity and a misguided policy.

While the Commission requests comments on a myriad of proposals, it is clear that only a prescriptive approach to access reform can provide immediate benefits to consumers and stimulate competition in local markets. First, as a matter of law, while the Commission should certainly consider the views of state regulators along with other commenters, the Commission has exclusive jurisdiction over interstate access reform. Furthermore, given that this proceeding is the only part of the trilogy that is purely interstate in nature, it can reform the current access regime independent from the scheduled separations reform proceeding.

The Commission can prescribe that access charges, which are currently \$11.6 billion too high, immediately be lowered by setting interstate access rates at economic cost, and then reinitializing actual price indices, price cap indices, and service basket indices to 100. A prescriptive approach can be implemented immediately,

accelerating competition in both local and long distance markets, and immediately bringing the benefit of lower rates to consumers. The Commission can accomplish this task with a minimal regulatory effort by relying on publicly available estimates of the economic cost of the elements used to provide switched access services. TELRIC estimates made by proxy cost models, such as the Hatfield Model employed by MCI and AT&T, may be used to reach a reasonable approximation of the forward looking cost of services residing in existing price cap baskets.

Bringing down access charges to forward-looking economic cost is not an unconstitutional taking of property. Access costs that reflect forward-looking cost will not deny incumbent LECs an opportunity to earn reasonable profits, and contrary to the financial doom predicted by the incumbent LECs, investors and financial analysts recognize that any financial impact of access reform will most likely be offset by the new opportunities that await the incumbent LECs in long distance, video, and other competitive markets once the incumbent LECs stop erecting barriers to local competition.

As a matter of competition policy, the Commission must set interstate access charges at forward-looking economic cost in order to guarantee just and reasonable rates and reduce the ability for anticompetitive cross-subsidy. If access charges remain above cost, MCI and other long distance carriers will be subsidizing the business of our soon-to-be-rivals, the incumbent LECs. Unless the Commission eliminates these subsidies, the incumbent LECs will be able to use these excessive charges to solidify their control over local markets or subsidize their entry into long distance. Either

outcome will seriously undermine the pro-competitive and pro-consumer goals of the Telecommunications Act of 1996.

Similarly, reliance on the proposed market-based approach to achieve access reform, coupled with additional pricing flexibility for the incumbent LECs, will negatively impact both local and long distance competition. Using a market-based approach in a market that remains a virtual monopoly is destined to fail from the perspective of both new entrants and end users, leaving the incumbent monopolist as the only beneficiary. As the attached affidavit of Dr. John E. Kwoka illustrates, premature deregulation of monopoly incumbent LECs and a reliance on "market-based" pricing can lead to adverse effects on consumers, inefficient entry, diminished market competition, and paradoxically, to the need for more -- not less-- regulatory oversight.

While appearing to embrace the pro-competitive thrust of the interconnection order, the Notice ignores the fact that the so-called market approach will permit incumbent LECs to substantially exercise their market power. Reliance on the market approach also subverts the policy goal of maximizing competition by encouraging efficient entry in as many different ways as possible. The market-based approach put forth in the Notice plainly encourages facilities based competition and the use of unbundled network elements to the exclusion of all other means. Resellers would see no access relief and there is no recognition that deploying facilities will take time with access remaining inflated in the interim. Furthermore, while unbundled network elements may eventually represent an important competitive restraint, the Notice places an unwarranted reliance upon these untested devices.

MCI proposes two principles that should guide the Commission when it considers the rate structure for access charges. First, the rate structure must reflect the way costs are incurred. This means that traffic sensitive (TS) costs must be recovered by TS rates and non-traffic sensitive (NTS) costs by NTS rates. This also implies that any TS rates must be assessed on the type of demand that is relevant, e.g., per-minute or per-line. Second, any rate structure must be auditable. The Commission must assure that access customers must be able to verify their access bills. Without this ability, access customers will be find themselves in the situation of having no choice but to trust the LECs, against whom they soon may be trying to compete.

MCI has historically led the way by lowering its long distance prices to consumers well above and beyond the limited access reductions ordered by the Commission. Competition in the long distance industry, with hundreds of companies offering services to consumers, acts as a guarantor that access reductions will be passed through to consumers in the form of lower long distance rates. History proves this to be the case, as long distance prices have fallen twice as much as access reductions. MCI pledges that when the overcharges for access are abolished, MCI will pass on the savings to our customers.

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and Pricing)	
)	
Usage of the Public Switched)	CC Docket 96-263
Network By Information Service)	
and Internet Access Providers)	

I. Introduction

MCI hereby submits its comments in the above referenced docket.¹ With this proceeding, the Federal Communications Commission (Commission) embarks on the final chapter of the competitive trilogy. The three proceedings that make up the trilogy -- interconnection, universal service and access reform -- are each critical to achieving the ultimate goal of a fully competitive local telecommunications marketplace which provides the public with lower prices, increased innovation, and ever-improving service.

¹ In the Matter of Access Charge Reform, CC Docket No. 96-262; Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1; Transport Rate Structure and Pricing, CC Docket No. 91-213, Usage of the Public Switched Network by Information Service and Internet Access Providers, CC Docket No. 96-263, Notice of Proposed Rulemaking, Third Report and Order, and Notice of Inquiry, FCC 96-488, released December 24, 1996 (Notice).

In the interconnection proceeding, the Commission wisely recognized that the Telecommunications Act of 1996² mandated rules that foster competition by eliminating impediments and by opening up monopoly network functions to new entrants at rates that allow efficient competitors to succeed in the market. The Commission therefore constructed a system permitting entry through the purchase of unbundled network elements priced at forward-looking costs and reasonable resale discounts on retail services.³ The Federal-State Joint Board on universal service similarly found that the use of a forward-looking cost model to size a competitively neutral universal service fund was necessary to achieve the important goals of universal service without harming the prospects for meaningful, effective local telephone competition.⁴

The Commission now addresses another fundamental part of the road toward local competition through access reform. The important principles, including the use of forward-looking economic costs, that were the underpinning

² Telecommunications Act of 1996, Pub. L. No. 104-104, 110 Stat. 56 (1996 Act), to be codified at 47 U.S.C. §§ 151 et. seq.

³ See, Implementation of the Local Competition Provisions in the Telecommunications Act of 1996, First Report and Order, CC Docket No 96-98, 11 FCC Rcd 15499 (1996) at 12. (Local Competition Order), Order on Reconsideration, CC Docket No. 96-98, 11 FCC Rcd 13042 (1996) (Local Competition Reconsideration Order), petition for review pending and partial stay granted, sub nom. Iowa Utilities Board et. al v. FCC, No. 96-3321 and consolidated cases (8th Cir. Nov. 1, 1996).

⁴ In the Matter of Federal-State Joint Board on Universal Service, CC Docket No. 96-45, Recommended Decision, FCC 96J-3 (rel. Nov. 8, 1996) (Joint Board Recommended Decision) at para. 270.

of the previous decisions and the key to establishing local competition must not be discarded now.

The fact that access charges are far in excess of cost is absolutely clear. In the Notice at issue here, the Commission expressly recognizes this to be the case.⁵ MCI therefore maintains that only a prescriptive approach will eliminate all of the subsidies from access charges and move everyone closer to just, reasonable and affordable rates for all telecommunications services, including access.

The incumbent local exchange carriers (LECs) have overstated the financial effect on them of reducing access to cost. Just as the Commission recognizes that access charges are full of unwarranted subsidies, so does the investor community. In fact, the financial analysts are anticipating access charge reductions.⁶ However, they also realize that the potential impact on the cash flow and revenues of the incumbent local monopolists will be more than offset by the new opportunities that await them in long distance, video and other competitive markets once the incumbent LECs stop erecting barriers to local competition.⁷ Furthermore, forcing one segment of the industry to overpay for a

⁵ Notice at para. 41 et. seq.

⁶ See e.g., Morgan Stanley, U.S. Investment Research, "Telecommunications Services: Can You Make Money Competing in the Local Market?" December 4, 1996 at 2.

⁷ See e.g., Smith Barney, "Telecommunications Companies - Outlook" November 22, 1996 at 2.

service to protect another segment of the industry is contrary to the spirit, intent, and plain language of the 1996 Act. The Commission should reject any arguments designed to insulate the incumbent carriers from their own poor investments and inefficient operations unless it is also prepared to consider the amount of earnings in excess of the authorized rate of return and scrutinize the financial books of these companies since divestiture.

While the Commission should not be establishing policy based on concerns about stock market reaction, a review of the most recent financial results for the incumbent LECs' extremely strong growth indicate there is no legitimate reason for concern.⁸ The major areas of growth will be largely unaffected by bringing access charges down to their economic cost. Line growth, including second lines which comes with very little incremental cost for the incumbent LECs, has achieved record levels.⁹ Another major growth area which comes at very little cost to the LEC is vertical services. These are services

⁸ "...[T]he economy continues to accelerate core demand growth to record levels, and price regulation continues to be an incentive for RBOCs to cut costs and drive revenue growth by selling more units and packages of 'vertical' services such as second lines, Caller ID and Voice mail, etc." (First Call Market Note, Industry Overview, Merrill Lynch, January 7, 1997.)

⁹ Second line sales for Bell Atlantic were up 24 percent through 1996 (First Call Market Note, Dean Witter Reynolds Equity Research, January 22, 1997); SNET saw an increase in second line sales of 29.3 percent (First Call Market Note, Bear, Stearns & Co. Inc. Equity Research January 23, 1997; SBC saw record in lucrative business line growth of 8.6 percent in the 4th Quarter while 60 percent of all new residential lines were second lines (First Call Market Note, Merrill Lynch, January 22, 1997.)

which are being marketed aggressively and provide the incumbent LECs with very large profit margins.¹⁰ Both the facts and the analyst's projections indicate the Commission need not be concerned about the overall financial health of the local monopolies and should not compromise on the appropriate pro-competitive, pro-consumer policy of bringing access charges down to economic cost.

This is the only proceeding in which the Commission is in a position to deliver on the real promise of competition for the public -- lower telecommunications prices. All of the important work that has been done to implement the 1996 Act thus far is premised on the fact that consumers will benefit from increased competition and lower rates. The access charge proceeding, however, presents an opportunity for the Commission to provide a consumer benefit -- lower long distance prices -- right now. The fact that this action would also help bring competition to the local monopoly market makes any other action both a missed opportunity and a misguided policy.

Consistent with our pro-competitive, pro-consumer history, MCI has historically led the way by lowering its long distance prices to consumers well above and beyond the limited access reductions ordered by the Commission.

¹⁰ For instance, Bell Atlantic saw caller ID revenues nearly double in 1996 and Return Call revenues increased by 40 percent. (First Call Market Note, Dean Witter Reynolds Equity Research, January 22, 1997); SBC's vertical services, including voice mail and Caller ID, grew by 22.6 percent. (First Call Market Note, Merrill Lynch, January 22, 1997); Ameritech increased its vertical service promotions resulting in significant increased growth (8.5 percent) in per line revenue. (First Call Market Note, Merrill Lynch, January 14, 1997.)

The competition in the long distance industry, with hundreds of companies offering services to consumers, acts as a guarantor that access reductions will be passed through to consumers in the form of lower long distance rates.¹¹ History proves this to be the case, as long distance prices have fallen twice as much as access reductions.¹² MCI pledges that when the overcharges for access are abolished, MCI will pass on the savings to our customers.

In these comments, MCI will demonstrate why a prescriptive approach to access reform is necessary to provide immediate benefits to consumers and stimulate competition in local markets, both as a matter of law and sound public policy. The Comments will also demonstrate the shortcomings of using a market-based approach to achieve access reform and the negative effect it will have both on local and long distance competition. Then, we will illustrate in greater detail the dangers of the premature and excessive pricing flexibility outlined in the Notice. MCI will also explain the basis for the gap between embedded and forward-looking costs and present a series of steps the Commission can take to eliminate it. Finally, the comments address the proposed rate structure modifications from the Notice.¹³

¹¹ Hall, Robert E., "Long Distance: Public Benefits from Increased Competition," 1995.

¹² Federal Communications Commission, "Telecommunications Industry Revenue: TRS Fund Worksheet Data", December 1996.

¹³ The FCC should also recognize that a period of "fresh look" is appropriate for all access agreements in light of the fundamental changes to rates and

II. A Prescriptive Approach to Access Reform Is Necessary to Protect the Development of Local Competition and Preserve Long Distance Competition.

In 1984, the Commission established the current access charge regime.¹⁴

The charges were based on the embedded costs of the incumbent LECs and were designed to compensate the local monopoly for use of their facilities. The incumbent LECs have never been forced to show that these charges reflect forward-looking economic costs. With the 1996 Act, the standard has changed. The Commission must require the incumbent LECs to justify access charges based on forward-looking costing principles to send appropriate pro-competitive signals to the local access market.¹⁵

Under the new Telecommunications Act and the rules implementing it thus far, there is absolutely no economic or policy justification for continuing above cost access charges. Approximately 40 cents of every long distance dollar is returned to the local monopoly telephone companies in the form of access charges.¹⁶ The actual economic cost of providing access, using the

rate structures that are likely to result from this proceeding.

¹⁴ In the Matter of MTS and WATS Market Structure, Third Report and Order, CC Docket No. 78-72, Phase I, 93 F.C.C. 2d 241 (1983).

¹⁵ This will be especially important once the incumbent LECs get into the long distance market because they will be providing access services to their own long distance affiliate and incur only the economic cost of providing access. At the same time, competitors will be forced to pay inflated access charges leading to discriminatory rates.

¹⁶ "Telecommunications Industry Revenue: TRS Fund Worksheet Data" at 9; See also, Competitive Telecommunications Association v. FCC et. al., 87

same forward-looking methodology employed by the FCC in the interconnection proceeding and recommended by the Federal State Joint Board on Universal Service, is only about 5 cents of every long distance dollar.

Interstate access charges are \$11.6 billion too high. This includes \$6.6 billion in excessive "costs" and about \$5 billion in universal service support that should be recovered in a competitively neutral fashion. The result is that the average long distance customer is paying approximately \$6.00 per month too much for long distance service, which goes to line the pockets of the incumbent LECs.¹⁷ Any approach to reform that permits the incumbent LECs to continue to receive these uneconomic subsidies would certainly fail the Act's public interest test as well as the requirement that rates be just, reasonable and affordable.¹⁸ To achieve the goal of effective competition in the local market, the Commission must eliminate this excess immediately through the use of a prescriptive approach. Furthermore, the Commission should not even begin to consider whether the competitive checklist has been met until the excess is removed from access.

F.2d. 522 (D.C. Cir.)

¹⁷ Even if interstate access charges recover the full \$5 billion in universal service support, this still means access charges are recovering \$6.6 billion more than necessary.

¹⁸ 47 U.S.C. 201(b); See also, 47 U.S.C. 251-52; 254(b)(5) and 254(k).

A. A Prescriptive Approach to Access Reform Is the Quickest and Easiest Route to Economically Rational Pricing and Maximum Competition.

Bringing access down to forward-looking economic cost is critical both as a matter of competition policy and as a matter of law. The law requires that, the Commission ensure rates are just and reasonable¹⁹ and that all implicit subsidies are made explicit.²⁰ The Commission has recognized that at least some of the excess contained in the access charge regime is being used to fund universal service.²¹ The Commission must identify the economic cost of providing universal service as well as access. Once the competitively neutral universal service fund is established, access charges must be reduced by an amount equal in size to the universal service contribution currently made in access charges. Failure to do so could lead to a double recovery for the incumbent LEC, once through the universal service fund, and a second time through collection of artificially inflated CCL and the completely unnecessary TIC charges.

In addition, to guarantee just and reasonable rates and reduce the ability for anti-competitive cross-subsidy, the Commission must disallow recovery of all

¹⁹ Id.; See also, 47 U.S.C. 205(a).

²⁰ 1996 Act at §254.

²¹ See, Local Competition Order at para. 719 "...the CCLC and TIC, which in part represent contributions toward universal service..."

access charges above forward-looking economic cost. In the past, an argument could be made that while excessive access charges were unfair, they had no anti-competitive effect because the incumbent LECs could not provide competitive long distance services. Today, however, the competitive threat is clear. If access remains above cost, MCI and the other long distance carriers will be subsidizing the business of our soon-to-be rivals, the incumbent LECs. Unless the Commission eliminates excessive charges, the incumbent will be able to use them to solidify their control over their local markets or subsidize their entry into long distance. Either outcome will seriously undermine the pro-competitive and pro-consumer goals of the law.

Once the hidden subsidies to support universal service are made explicit as required under the 1996 Act,²² there is absolutely no legitimate reason to permit the incumbent LECs to charge above the forward-looking economic cost for access. As indicated supra, any access charges that remain above cost will plainly violate the Act's requirement that rates be just and reasonable. Only a prescriptive approach to access reform can eliminate these excess charges immediately, delivering benefits to captive ratepayers and clearing another road-block to vigorous competition in all telecommunications markets.

As MCI will demonstrate throughout these comments, the multi-phased market-based approach to access reform outlined in the Notice would not only

²² 47 U.S.C. 254(b)(5).

thwart the development of local competition and force captive telephone ratepayers to continue to subsidize some of the wealthiest corporations in the country, but it would also create an unnecessary regulatory morass. Such an approach would require the Commission to establish general standards for different levels of pricing flexibility, actively monitor the behavior and business practices of the incumbent LECs in both the local and interstate markets, and review claims by the incumbent LECs that they meet the requirements for phase 1, 2, or 3 of access reform.

Using a prescriptive approach, on the other hand, will permit the Commission to fix a very broken system and enable competition to take hold in all markets by removing all subsidies immediately. Once the subsidies are squeezed out of the access system, the Commission can establish a relatively simple and objective measurement of effective competition that can lead to the ultimate deregulation of access charges.

All of the damage that would be done to the development of a competitive local market and the competitive long distance market by allowing the incumbent LECs to retain uneconomic subsidies can be eliminated through a prescriptive approach to access reform.

B. Reform Requires the Use of Consistent Costing and Pricing Principles.

Access reform represents the last piece of the competitive telecommunications trilogy. As the Commission and Federal-State Joint Board

have recognized in the interconnection and universal service proceedings respectively, the availability of network elements and services at their forward-looking economic cost is critical to the development of competition. All of the pro-competitive steps taken in the other key proceedings that rely on this basic costing principle, are threatened if the incumbent LECs are permitted to continue to collect huge subsidies from access.

There is no rational justification for permitting the incumbent LECs to continue to collect excessive access charges. Using different costing principles will permit the incumbent LECs to change the source of the unwarranted subsidies currently received from access without taking the monies out of the system as is necessary to allow competition to flourish in all markets. The result may be simply changing which customers at any given time are being forced to pay the subsidy instead of eliminating it.

C. The Commission Has an Opportunity to Truly Level the Playing Field with this Proceeding.

Today, only the incumbent LECs enjoy the comforts of monopoly. One of the primary goals of the 1996 Act was to eliminate this last monopoly and all of the associated benefits in an effort to bring vigorous competition to all markets once and for all. Just as AT&T has learned since 1984, while there are risks in the competitive market, there are even greater rewards. The days of being able to earn great rewards with little or no risk for the incumbent LECs must end under the 1996 Act. An essential part of this process is the elimination of the

funds that can and will be used to disadvantage new entrants or are used for anti-competitive cross-subsidy.

The job of effectively monitoring and protecting against cross-subsidy is getting more difficult every day. As the telecommunications marketplace continues to expand and the incumbent LECs enter new business both in and out of the industry, the Commission will have an increasingly difficult time following the money trail. The shared jurisdiction with states makes it possible for the incumbent LECs, especially the Regional Bell Operating Companies (RBOCs), to play a shell game which effectively keeps well intentioned regulators at all levels of government from identifying illegal and anti-competitive cross-subsidy.

The surest way to eliminate anti-competitive conduct and cross-subsidy is to eliminate the funds that make it possible. The \$11.6 billion in excess revenues LECs obtain profits from access charges is a major source of these funds. Only a prescriptive approach will squeeze these funds out of the system anytime soon and prevent the anti-competitive effects of these subsidies from skewing competition in a variety of markets.

D. A Prescriptive Approach Creates Certainty for All Parties.

Concern about the financial effect on the incumbent LECs of bringing access down to cost should be irrelevant to the Commission and is, nonetheless, completely overblown. Incumbent LEC claims ignore the new revenue opportunities that are or will soon be available to them. Furthermore, they are

based on the assumption that the incumbent LECs are entitled to everlasting monopoly profits. The writing has long been on the wall that the old monopoly regime, with access rates far exceeding costs, would not be permitted to continue. Investors recognize, and have already taken into account, the new risks and opportunities associated with ownership of an incumbent LECs stock.

There are significant benefits to the industry, including the incumbent LECs, from a prescriptive approach as well. Companies will not have to waste resources on legal challenges to Commission actions including necessary access charge reductions and whether or not the requirements for the different phases of relief under a market-based approach to reform have been met. These are funds that MCI would rather use to make investments that help facilitate entry into new markets.

A prescriptive approach also provides certainty for all parties, including the incumbent LECs and their investors, as they make their business plans and take steps to enter in-region long distance and other markets. The elimination of funds which could be used to cross-subsidize incumbent LEC entry into the competitive long distance business will eliminate one hurdle to local entry and should only help the regulators at all levels as they make the required determination of whether the requirements for in-region long distance entry have been met.

This proceeding should lead the Commission to close the doors to unfair and anti-competitive conduct by the incumbents before trying to open the doors

to competition and taking a hands off approach to the access charges paid to local monopolies. No matter how hard we try, none of us can wish away the monopoly. Access policy should not be premised on our hopes for a competitive local market in the future. Rather, the Commission should use a prescriptive access reform policy to help achieve this important objective.

III. Executing The Prescriptive Approach To Access Reform

A. Driving Access Rates to Cost Requires the Commission to Utilize Existing Price Cap Mechanisms to Replicate Economically Efficient Rates.

MCI supports the Commission's goal of... "requir[ing] LECs to move prices for interstate access in their service areas to more economically-efficient levels..."²³ MCI advocates the Commission adopt a prescriptive approach to achieve this goal. As our comments demonstrate in Section V infra., a market-based approach is incapable of moving access rates to economically efficient levels, and must be rejected. Since its adoption of price cap regulation, the Commission has sought to set rates for regulated carriers at economically efficient levels by replicating competitive outcomes. The Commission has recognized that setting rates at economically efficient levels will benefit not only consumers of incumbent LEC services, but also the incumbent LECs themselves, by making them stronger and more productive competitors.²⁴ This

²³ Notice at para. 16.

²⁴ "If we can design a regulatory system for these carriers' access business that mirrors the efficiency incentives found in competitive markets, we will

latter goal has become more important in light of new market opportunities for LECs.

When the Commission adopted price cap regulation for the LECs in 1990, it presumed that rates were at reasonable levels. However, it never determined whether the costs that formed the basis of LEC rates, and ultimately LEC actual price indices (API), were set at economically efficient levels.²⁵ The Commission recognized that these initial rates were not based on economically efficient costs, but were "...the best that rate of return regulation can produce."²⁶

The Commission sought to minimize the risk that LEC interstate customers would pay rates above economically efficient levels by: first, limiting the rate of actual price changes to economically efficient rates of change in prices; and second, adopting a variety of sharing and adjustment mechanisms. The Commission did not explicitly identify a mechanism through which initial rates would be adjusted downward to economically efficient levels, but it believed that the incentives inherent in price cap regulation, including the consumer

have put in place a system that will go a long way toward making the LECs stronger, more productive competitors for all the markets in which they must operate. LEC Price Cap Order, 5 FCC Rcd at para. 33.

²⁵ "...we are not making a finding that existing rates are just and reasonable, but only that they are a reasonable starting point for price cap...." *Id.*, at para. 241.

²⁶ *Id.* at para. 232.

productivity dividend, would eventually bring rates to economically efficient levels.²⁷

Abstaining from setting initial rates for LEC interstate access services that were economically efficient, while understandable given the lack of reliable economic models estimating efficient costs at the time, has required the Commission to periodically true-up, or reinitialize, LEC interstate rates. The Commission recognized this need when it initiated its Price Cap Performance Review for Local Exchange Carriers.²⁸

In this Notice, the Commission recognized the need to bring LEC access rates to economically efficient levels in a manner compatible with regulations adopted pursuant to its implementation of the 1996 Act.²⁹ MCI demonstrates that a market-based approach will not accomplish this goal, or will do so only at significant regulatory expense and involvement (See V infra). Instead, the Commission must adopt a prescriptive approach. A prescriptive approach can be implemented immediately, accelerating competition in both local and long distance markets, and immediately bringing the benefit of lower rates to consumers.

²⁷ "While we agree that rates produced by a rate of return system can be uneconomically high, it is the ongoing operation of price cap regulation that will produce lower rates..." *Id.*, at para. 242.

²⁸ Price Cap Performance Review for Local Exchange Carriers, CC Docket No. 94-1, First Report and Order, 10 FCC Rcd 8961; March 30, 1995.

²⁹ Notice at para. 5.